

**Letter of Findings Number: 09-0259
Indiana Sales and Use Tax
For 2006 and 2007**

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ISSUES

I. Sales and Use Tax— Imposition.

Authority: IC § 6-2.5-1-1 et seq.; IC § 6-2.5-2-1; IC § 6-2.5-3-2; IC § 6-2.5-3-4; IC § 6-2.5-5-27; IC § 6-8.1-5-1(c); Indiana Dep't of State Revenue v. Kimball Int'l Inc., 520 N.E.2d 454 (Ind. Ct. App. 1988).

Taxpayer protests the assessment of use tax on a variety of purchases.

II. Ten-Percent Negligence Penalty.

Authority: IC § 6-8.1-5-1(c); IC § 6-8.1-10-2.1(a)(3); IC § 6-8.1-10-2.1(d); [45 IAC 15-11-2\(b\)](#); [45 IAC 15-11-2\(c\)](#).

Taxpayer asks the Department to exercise its discretion to abate the ten-percent negligence penalty on the ground that taxpayer believed it interpreted the applicable statutes correctly.

STATEMENT OF FACTS

Taxpayer is an Indiana corporation operating rent-to-own stores in Indiana and three other states. Taxpayer's stores carry a variety of home appliances, electronics, and home furnishings for sale or rent. Taxpayer also sells satellite radio subscriptions and prepaid cellular phones. Taxpayer's business operations include use of a related transit company (Transit) to transport taxpayer's property.

For the 2006 and 2007 tax years ("Tax Years"), the Department of Revenue (Department) conducted an audit review of taxpayer's business records and tax returns. The Department's audit found some invoices that were billed to Transit. The invoices corresponded to purchases paid from an account common to both Taxpayer and Transit. Transit did not pay sales tax on these purchases, claiming sales tax exemptions based upon an assertion that Transit was predominantly engaged in public transportation. As a result of the audit, the Department disallowed the public transportation exemption and assessed additional amounts of sales and use tax. Taxpayer disagreed with the Department's assessments and submitted a protest to that effect. An administrative hearing was conducted during which taxpayer explained the basis for its protest. This Letter of Findings results.

I. Sales and Use Tax— Imposition.

DISCUSSION

Pursuant to IC § 6-8.1-5-1(c), all tax assessments are presumed to be accurate, and the taxpayer bears the burden of proving that an assessment is incorrect.

IC § 6-2.5-2-1 provides:

(a) An excise tax, known as the state gross retail tax, is imposed on retail transactions made in Indiana.

(b) The person who acquires property in a retail transaction is liable for the tax on the transaction and, except as otherwise provided in this chapter, shall pay the tax to the retail merchant as a separate added amount to the consideration in the transaction. The retail merchant shall collect the tax as agent for the state.

IC § 6-2.5-3-2(a) provides:

An excise tax, known as the use tax, is imposed on the storage, use, or consumption of tangible personal property in Indiana if the property was acquired in a retail transaction, regardless of the location of that transaction or of the retail merchant making that transaction.

Accordingly, Indiana imposes a sales tax on retail transactions and a complementary use tax on tangible personal property that is stored, used, or consumed in the state. IC § 6-2.5-1-1 et seq. An exemption from the use tax is granted for transactions where the gross retail tax ("sales tax") was paid at the time of purchase pursuant to IC § 6-2.5-3-4.

During the audit, taxpayer submitted a number of invoices billed to Transit that did not include payment of sales tax. Transit purchased fuel, replacement parts, and repair services Transit characterized as vehicle expenses associated with its transportation business. Taxpayer maintains that these purchases were exempt under the public transportation exemption found at IC § 6-2.5-5-27.

IC § 6-2.5-5-27 provides:

Transactions involving tangible personal property and services are exempt from the state gross retail tax, if the person acquiring the property or service directly uses or consumes it in providing public transportation for persons or property.

In applying any tax exemption, the general rule is that "tax exemptions are strictly construed in favor of taxation and against the exemption." Indiana Dep't of State Revenue v. Kimball Int'l Inc., 520 N.E.2d 454, 456 (Ind. Ct. App. 1988).

Taxpayer asserts that it never owned or operated any delivery vehicles used to transport items to its

customers during the Tax Years. Instead, taxpayer entered into a Transportation Agreement with Transit whereby Transit provided for-hire motor contract carrier services in exchange for a fee. Under the Transportation Agreement, Transit transported and delivered taxpayer's merchandise to taxpayer's customers. Taxpayer included a copy of this Agreement with its protest.

During the hearing, the Department requested additional documents and information from Taxpayer to support Taxpayer's arguments regarding the bifurcation of Taxpayer's and Transit's activities. Taxpayer subsequently submitted a number of documents further detailing ownership and maintenance by Transit of vehicles, as well as displaying distinct separation of Transit's business purpose from that of Taxpayer. Based upon the information provided, Taxpayer has met its burden of showing Transit as a separate and distinct entity. Therefore, for the Tax Years, Transit can claim the public transportation exemption for those purchases it characterizes as vehicle expenses associated with its transportation business.

FINDING

Taxpayer's protest is sustained.

II. Ten-Percent Negligence Penalty.

DISCUSSION

Taxpayer believes that it is entitled to abatement of the ten-percent negligence penalty because it had a reasonable cause for its position that Transit made tax exempt purchases based upon the belief that Transit engaged in public transportation for taxpayer.

Under IC § 6-8.1-5-1(c), "[t]he burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is made." An assessment – including the negligence penalty – is presumptively valid.

IC § 6-8.1-10-2.1(a)(3) requires that a ten-percent penalty be imposed if the tax deficiency results from the taxpayer's negligence. IC § 6-8.1-10-2.1(d) states that, "[i]f a person subject to the penalty imposed under this section can show that the failure to... pay the full amount of tax shown on the person's return... or pay the deficiency determined by the department was due to reasonable cause and not due to willful neglect, the department shall waive the penalty."

Departmental regulation [45 IAC 15-11-2](#)(b) defines negligence as "the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer." Negligence is to "be determined on a case-by-case basis according to the facts and circumstances of each taxpayer." Id.

IC § 6-8.1-10-2.1(d) allows the Department to waive the penalty upon a showing that the failure to pay the deficiency was based on "reasonable cause and not due to willful neglect." Departmental regulation [45 IAC 15-11-2](#)(c) requires that in order to establish "reasonable cause," the taxpayer must demonstrate that it "exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed...."

The Department is prepared to agree that taxpayer had a "reasonable" cause to believe that neither it nor Transit was required to pay sales or use tax on the purchase of vehicles, fuel, and replacement parts.

FINDING

Taxpayer's protest is sustained.

CONCLUSION

Taxpayer is sustained as to the substantive issue of applicability of the public transportation exemption to purchases a related transit company characterizes as vehicle expenses associated with its transportation business. Taxpayer is also sustained as to its protest of the negligence penalty.

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